

Message Text

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ACTION EA-10

INFO OCT-01 EUR-12 ISO-00 AID-05 CIAE-00 COME-00 EB-07

FRB-03 INR-07 NSAE-00 TRSE-00 XMB-02 OPIC-03 SP-02

CIEP-01 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04

CEA-01 L-02 H-02 /088 W

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P R 010900Z APR 75

FM AMEMBASSY JAKARTA

TO SECSTATE WASHDC PRIORITY 7327

INFO AMEMBASY BONN

AMCONSUL HONG KONG

AMEMBASSY LONDON

AMCONSUL MEDAN

AMEMBASSY PARIS

AMEMBASSY SINGAPORE

AMCONSUL SURABAYA

AMEMBASSY TOKYO

C O N F I D E N T I A L JAKARTA 3837

HONG KONG FOR TREASURY REPRESENTATIVE

EO 11652: GDS

TAGS: EFIN ENRG EALR ID

SUBJ: FURTHER DECISIONS ON FUTURE SHAPE ON PARTAMINA ACTIVITIES

REF: A. JAKARTA 3195 B. JAKARTA 3328 C. EAL

1. SUMMARY: PRESIDENT SUHARTO MARCH 24 INSTRUCTED
MINISTER FOR ADMINISTRATIVE REFORM, DR SUMARLIN, TO
ASSUME FULL RESPONSIBILITY FROM PERTAMINA FOR MASSIVE
KRAKATAU STEEL PROJECT WHICH CONTRIBUTED HEAVILY TO
PERTAMINA'S PRESENT FINANCIAL PROBELMS. PRESIDENT
ALSO REPORTEDLY REQUESTED BANK INDONESIA GOVERNOR,
IN REVIEWING PERTAMINA PROJECTS, TO IDENTIFY THOSE
OUTSIDE OF OIL SECTOR, FOR TRANSFER FROM PERTAMINA
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DIRECTION. MEANWHILE GOVERNMENT ACTIONS HAVE LARGELY

ALLAYED IMMEDIATE CONCERNS OF FOREIGN BANKS BUT DELAYS
IN ACTING ON PERTAMINA'S LARGE ARREARS TO
LOCAL AND FOREIGN SUPPLIERS CREATES CONTINUED
CONCERN. END SUMMARY

2. FOLLOWING FROM RELIABLE SOURCE CLOSE TO MINISTER SUMITRO:
ON MARCH 22 RESEARCH MINISTER SUMITRO MADE
DETAILED PRESENTATION TO PRESIDENT SUHARTO OF PAST
PERTAMINA FINANCING AND PROJECT DECISIONS AND THEIR
ADVERSE EFFECTS ON GOI FX RESERVES AND DEVELOPMENT
PROGRAM. PRESIDENT REPORTEDLY WAS DISMAYED AND
ANGRY TO LEARN THAT CONTRACTS WITH GERMAN SUPPLIERS
ON KRAKATAU PROJECT FAR EXCEEDED COST AND SCOPE
WHICH HE SAID IBNU ASSURED HIM WERE PLANNED, AND
WAS ESPECIALLY PIQUED BY CONTRACTS ON EXECUTIVE
HOUSING AT KRAKATAU THAT EXCEEDED BY THREE TIMES
GOI'S COST FOR NEW HOMES FOR ITS MINISTERS LAST
YEAR.

3. ON MARCH 24 PRESIDENT SUHARTO SUMMONED MINISTER
FOR ADMINISTRATIVE REFORM DR SUMARLIN AND INSTRUCTED
HIM TO ASSUME FULL RESPONSIBILITY FOR KRAKATAU PROJECT,
WITH AUTHORITY (A) TO CANCEL, STRETCH OUT, AND
RENEGOTIATE WHATEVER ASPECTS OF PROJECT HE FOUND
WARRANTED IT, (B) TO HIRE WHATEVER EXPERTS WERE
NECESSARY TO ASSIST HIM, AND (C) TO FIRE KRAKATAU
DIRECTOR MARJOENI SHOULD HE NOT BE FULLY COOPERATIVE.
PRESIDENT THEN CALLED IN GENERAL IBNU AND GENERAL
SUDHARMONO, (HEAD OF PALACE SECRETARIAT AND MEMBER
OF KRAKATAU BOARD OF DIRECTORS) AND REPEATED HIS
INSTRUCTIONS WITH SUMARLIN PRESENT. IBNU REPORTEDLY
WAS HALF APOLOGETIC AND HALF APOLOGIST, BUT
ACCEPTED DECISION. PRESIDENT SPECIFICALLY ORDERED
THAT PROJECT NOT EXCEED ORIGINAL PHASE I TARGET OF
500,000 TONS/YEAR (TPY) UNTIL FEASIBILITY AND
LONG TERM FINANCING FOR EXPANSION BEYOND THAT LEVEL
FULLY ESTABLISHED. (PROJECT HAD GROWN FROM \$500
MILLION TO AT LEAST \$1.9 BILLION, WITH 1.5 MILLION
TPY CAPACITY. WORLD BANK REPRESENTATIVE NOW
ASSISTING GOI TO DEVELOP LIST OF STEEL COMPANIES
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AND CONSULTANTS QUALIFIED TO ADVISE SUMARLIN, AND
EMBASSY HAS PROVIDED NAMES OF US FIRMS WITH INTEREST IN PROJECT.
WE EXPECT IBRD TO AVOID FINANCING OR OTHER DIRECT IN-
VOLVEMENT IN KRAKATAU REAPPRAISAL.

4. FROM SECOND-HAND SOURCES, WE UNDERSTAND PRESIDENT
HAS ALSO INSTRUCTED CENTRAL BANK GOVERNOR RACHMAT
SALEH, IN HIS REVIEW OF PERTAMINA DIRECTED PROJECTS,

TO IDENTIFY PROJECTS HE CONSIDERS OUTSIDE OIL SECTOR,
FOR PURPOSES OF TRANSFERRING THESE PROJECTS TO OTHER
MANAGEMENT.

5. WITH REGARD TO SETTLEMENT OF PERTAMINA OBLIGATIONS,
EMBASSY DISCERNs GENERAL SATISFACTION AMONG FOREIGN
BANK COMMUNITY WITH GOVERNMENT DECISIONS AND THEIR
PROMPT IMPLEMENTATION IN SHORT TERM BANK CREDIT
PROBLEMS. IN RELATED MATTER, PRESIDENT SUHARTO ALSO
ORDERED BANK INDONESIA TO ASSUME FROM STATE'S BANK
BUMI DAYA \$230 MILLION IN 6 MONTH BORROWINGS IT HAD
UNDERTAKEN FOR KRAKATAU PROJECT UNDER GOVERNMENT
GUARANTEE.

6. PROBLEM OF PERTAMINA ARREARS TO SUPPLIERS AND
CONTRACTORS NOW POSING PRESSING PROBLEM FOR GOI.
BANK INDONESIA NOW COMMITTED TO PAYING L/C'S AS
DUE AND SOME OFFSHORE SUPPLIERS HAVE SHIFTED FROM
L/C'S TO CASH-IN -ADVANCE ON PERTAMINA ORDERS. HOWEVER,
FOREIGN CONTRACTORS IN INDONESIA STILL FACE ARREARS
AVERAGING ROUGHLY 5 MONTHS, AND LOCAL SUPPLIERS AND
CONTRACTORS EVEN MORE SERIOUSLY AFFECTED. LAST WEEK
P T ASTRA, INDONESIA'S LARGEST PRIVATE CONGLOMERATE
WAS UNABLE TO MEET \$17.5 MILLION PAYMENT ON BANK DEBT AND
WAS FORCED TO NEGOTIATE ROLL-OVER. OTHER LOCAL FIRMS
ARE SAID TO BE FACING SUSPENSION OF ACTIVITIES BECAUSE
OF PERTAMINA PAYMENT ARREARS AND SLOWDOWN OF
ACTIVITIES. EMBASSY ALSO RECEIVED FINANCIAL COMMUNITY
REPORTS OF LARGE DEBTS OWED SUPPLIERS IN SINGAPORE.
BANK INDONESIA IN EARLY STAGES OF DETERMINING EXTENT
OF THESE PERTAMINA OBLIGATIONS, PRELIMINARY TO DECIDING
HOW TO DEAL WITH THEM. MOST URGENT CASES OF LOCAL
SUPPLIERS MAY REQUIRE EARLY STOP-GAP SOLUTIONS.
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7. COMMENT: REPORTED PRESIDENTIAL REACTIONS TO
MINISTER SUMITRO'S PRESENTATION IS CLEAREST INDICATION
WE HAVE TO DATE THAT PRESIDENT MAY NOW BELIEVE THAT
IBNU GREATLY EXCEEDED HIS BRIEF IN MAJOR DECISIONS
SUCH AS THOSE ON KRAKATAU PROJECT. MINISTER SUMITRO
REPORTEDLY ADVISED PRESIDENT THAT PETAMINA CRISIS
WOULD ADVERSELY AFFECT 1977 ELECTION PROSPECTS BY
SEVERELY CURTAILING GOVERNMENT DEVELOPMENT EFFORT.
SUMITRO SAID TO BELIEVE THAT PRESIDENTIAL SENSITIVITY
TO THIS ISSUE CONTRIBUTED TO DECISIVENESS OF
PRESIDENT'S REACTIONS AND SUBSEQUENT ASSIGNMENT OF
SIGNIFICANT ADDITIONAL DECISION-MAKING AUTHORITY TO
GOI ECONOMIC TEAM.

8. EMBASSY EXPECTS EXTENSIVE SURGERY ON KRAKATAU
PROJECT IN LIGHT OF EVIDENCE OF SOME CONTRACT COSTS UP
TO THREE TIMES THAT OF COMPETITIVELY AVAILABLE
ALTERNATIVES (EG SIEMENS POWER CONTRACTS).
NEWSOM

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